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SUBJECT: NEW TOURISM LAW A POSITIVE STEP, BUT CHALLENGES
REMAIN

1. SUMMARYSummary: In December 2005, the GOESel Salvador approved a Tourism Law establishing tax incentives for new investment in the sector. The law shows government support for the industry, but has received criticism from the International Monetary Fund (IMF). The GOES is expecting to close the year with \$629 million in tourist receipts from 1.4 million visitors, 32XX and 33XX percent increases over 2004, respectively. income as the result of 1.4 million tourists visiting El Salvador. If the forecast turns out to be right, then the sector will represent 3.8% of total GDP. The Tourism Ministry still faces the challenges of limited resources and staff, and there is weak financial support for the sector from the private sectorbanks. END SUMMARYEnd Summary.

2. On December 9, 2005, the Legislative Assembly approved a new tourism law to spur investment in the sector.. The new law, which the private sector has been calling for for years, takestook effect January 1, 2006, and establisheds fiscal tax incentives for tourist operators, and will take effect in January 2006. The incentives will benefit those enterprises thathose whocompanies that invest a minimum of \$50,000.00 in tourism tourism-related projects in El Salvador. Upon reaching the \$50,000.00 investment level, and the enterprise opens to the public, the incentives begin. Incentives include a 100 percentn income tax break of 100% for 10 years,, a land acquisition tax break for five years, and a 50 percent cut in municipal taxes for five years. The government will also foregowaive duties on imported goods used for construction or ongoing operations of goodsused in the project, related to the enterprise up to the amount of the investment. up to tThe total value of the investment. the exemption is based on the amount ofFor five years the enterprise also receives a land acquisition tax break, as well as a 50% cut in municipal taxes.In order tTo take advantage of these incentives, the enterprise investor will need tomust contribute 5% percent of profits during the exemption period to a government-administered Tourism Promotion Fund.

3. TIn a communiqu which was released by the Technical Secretary to the President, the International Monetary

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FunIMFd was in consultations with the Salvadoran Government from December 5 - 8, and has criticized El Salvador's the use of these types of fiscaltax incentives to attract investment, . The IMF recommending instead s that countries in the region develop a code of conduct to avoid a competition for investment based on tax incentivesin which fiscal incentives are used to attract investment, which the IMF says will weaken fiscal positions in the region. . President Sacas responded to this criticism in a newspaper interview by saying having the tourism law was better than no law at all. Comment: The Salvadoran Treasury Ministry of Finance also hexpressedad reservations about the law as tax breaks will decrease El Salvador's tax revenues, at a time when they are trying to increase tax collection, as it decreases the amount of funding they receive in tax revenues. However, President Sacas signed the law despite this criticism, saying publicly that the country could had no choice but to act quickly or lose potential for growth in the sector. [is this fair paraphrasing?] [There is also concern about the possibility of use of the exemptions for non-tourist related activities. Comment: The law is in line withsimilar to those of other countries in the region, who have used these types of incentives for years to promote their tourist industriesy. End Comment.]

Sector Overview

4. President Sacas has identified tourism as a high potential sector, and established a new Ministry of Tourism when he took office in June 2004. The Salvadoran Ministry of Tourism expects estimated that by the end of 2005, 1.4 million tourists willwould have visited El Salvador. The total income for the sector is expected to be \$629 million, representing 3.8% of total GDP. This would be an increase from 2004 figures of 966,000 tourists and \$425 million in revenue. [Can you compare 2004 to 2005, visitors and total receipts?] GovernmentGOES surveys indicate thatT the growth

in revenues is a result of reflects tourists' increasing their average lodging days from 5 days to 6 and while average and increasing average spending from spending grew from \$87/day to \$92 per /day as compared with last year 2004. The regional breakdown of tourist entries to El Salvador is as follows; ; Central America (69%), percent), followed by North America (25%), percent), Europe (3%) percent) and Asia (3%). percent). [Comment. The Salvadoran government does not provide separate figures for information to differentiate those people Salvadoran expatriates coming to El Salvador to visit family and friends from those others coming to visit on what is traditionally considered a vacation. Thus tThe figures are most likely very heavily skewed towards family visits, and it is impossible to verify how many travelers are coming to El Salvador as a tourist destination. The Ministry of Tourism should focus on traditional tourism activities as a goal; right now they are capturing large numbers of people who would be coming to El Salvador anyway and classifying them as tourists. End Comment.]

15. In 2006, The Tourism Ministry is now working on developing an Action Plan for the period 2006 - 2014. The Action Plan will include specific activities to promote new investment and attract more tourists. The goal of the GOES is that by the end of 2009 the tourism sector will represent at least 5% of total GDP. Another goal is to increase the availability of hotel rooms; by 2014 they want to double the number of rooms in the country to 12,000.

15. Tourism Minister Ruben Rochi has set new goals for the sector in 2006. He plans to finish the reconstruction of two important government government-managed tourist centers that are popular and commonly attended by low income users among domestic tourists (Los Chorrros and Amapulapa) but that were severely damaged during the 2001 earthquakes; he also wants to revitalize and promote the Port of La Libertad; create national tourism committees that would be in charge of managing the tourism issues at a municipal level; , and promote alternate tourism routes. The Ministry is also working on developing an Action Plan for the period 2006 - 2014 that will include specific activities to promote new investment and attract more tourists. By the end of 2009, the GOES hopes the tourism sector will represent at least 5 percent of GDP.

Challenges to Tourism Promotion

16. Need to add to this para on the ministry/budget. We say it is not enough, but don't say what the funding is, or that it is new and just getting started, etc.]
Currently, the Ministry does not have a technical staff or budget to perform the initiatives originally proposed. The new law establishes a source of badly needed income for the Ministry but budget constraints will continue to limit its projects. Its budget was reduced from \$7.5 million in 2005 to \$7.41 million in 2006 with the expectation that payments into the Tourism Promotion Fund (independent of the general budget) would make up for the decreased budget. For example, the Ministry has no funding to conduct a much-needed wants to do a National Survey survey of all tourism centers, hotels, and other locations, . but that is still a pending activity until the funds are received to do it. It is expected that The Tourism Promotion Fund (independent from the general budget), established in the new Tourism Law, will may prove a useful source of funding be the source of such funds. In addition to the investors' 5 percent The Tourism Promotion Fund will receive contribution, The Tourism Promotion Fund will be funded from an \$7 of the current increase in the airport tax of \$27.14 to \$32 airport tax and a 5 percent hotel tax will go the Tourism Promotion Fund. , of which \$7 will go directly to the fund. Other sources of revenue for the fund are a 5% hotel tax. The fund will also be used to develop advertising campaigns to attract international tourists. Still, the Ministry has no funding to conduct what it says is a much-needed national survey of all tourism centers, hotels, and other locations. Currently there are no such campaigns, even in the most obvious markets such as the United States.

1. 7. Another important challenge the sector faces is the lack of support from the local banking system. Currently, there are no specific credit lines to support the modernization of the sector; in addition, the banking system also lacks expertise to evaluate tourism projects. Now with the approved Law, the private sector will start with the investment plans they have in mind and for the banking system to create new credit lines for the sector.

187. Comment. Much has been made of a new all inclusive beach resort opened in December by a Colombian group, Decameron, but this is a single success. Apart from Tthe

sector policy, the industry has much to do in order to face serious obstacles to developing the image of El Salvador as a tourist destination; not many people think of El Salvador as a place for a vacation, and news reports on the emerging gang problem and rising violence only complicate the matter. Even though ~~Although~~ However, President Saca gave his ~~has~~ pledged his full commitment support to the development of the tourist sector in his inauguration ceremony in 2004, and the new Tourism Law is the first sign of active support for the sector by the government. If the GOES is going to support the development of this sector, it must assign the Ministry should be assigned more additional resources to hire a technical staff and work on the initiatives that are pending. It will also have to separate out people who are coming to El Salvador to visit family and friends from tourists who specifically choose El Salvador as a tourist destination, which will allow them to focus their efforts in light of severely constrained resources. End Comment.

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